

Message Text

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12

ACTION AF-08

INFO OCT-01 EUR-12 IO-13 ISO-00 CIAE-00 PM-04 H-02 INR-07

L-03 NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15 USIA-06

AID-05 COME-00 EB-07 FRB-03 TRSE-00 XMB-02 OPIC-03

CIEP-01 LAB-04 SIL-01 OMB-01 STR-04 CEA-01 FS-01

ABF-01 INT-05 /119 W

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P 150655Z JUL 76

FM AMEMBASSY LUSAKA

TO SECSTATE WASHDC PRIORITY 3649

INFO AMEMBASSY ABIDJAN PRIORITY

AMEMBASSY ACCRA PRIORITY

AMEMBASSY BRUSSELS PRIORITY

AMEMBASSY DAKAR PRIORITY

AMEMBASSY DAR ES SALAAM PRIORITY

AMEMBASSY GABERONE PRIORITY

AMEMBASSY KINSHASA PRIORITY

AMEMBASSY LAGOS PRIORITY

AMEMBASSY LONDON PRIORITY

AMEMBASSY MAPUTO PRIORITY

AMEMBASSY MASERU PRIORITY

AMEMBASSY MBABANE PRIORITY

AMEMBASSY NAIROBI PRIORITY

AMEMBASSY PARIS PRIORITY

AMEMBASSY PRETORIA PRIORITY

AMEMBASSY ROME PRIORITY

USMISSION USUN NEW YORK PRIORITY

DIA WASHDC PRIORITY

AMEMBASSY GENEVA PRIORITY

C O N F I D E N T I A L LUSAKA 1812

EO 11652: GDS

TAGS: EFIN

SUBJECT: DEVALUATION OF THE KWACHA

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REF: LUSAKA 1753

BEGIN SUMMARY: ANNOUNCEMENT OF DEVALUATION OF KWACHA JULY 8 WAS LONG EXPECTED WITH ONLY PERCENTAGE AND TIMING IN QUESTION. EXCEPT WITHIN EXPATRIATE COMMUNITY, INITIAL REACTION HAS BEEN MUTED. MINISTRY OF FINANCE HAS DOWNPLAYED ADVERSE EFFECTS AND APPEARS TO BE OVER-VALUING SHORT-TERM BENEFITS, ESPECIALLY IN TERMS OF ENCOURAGING GREATER USE OF LOCALLY PRODUCED GOODS. MEASURE DESCRIBED AS NECESSITATED BY SEVERE BOP PROBLEMS - BUT DEVALUATION UNLIKELY TO PROVIDE SIGNIFICANT RELIEF IN RELATION TO THE MAGNITUDE OF ZAMBIA'S FOREIGN EXCHANGE PROBLEMS. MAJOR BRUNT OF DEVALUATION WILL BE BORNE BY EXPATRIATE AND NON-ZAMBIAN RESIDENT COMMUNITIES. FORMER WILL SEE COST OF LIVING RISE SHARPLY AT SAME TIME THAT VALUE OF REMITTANCES ABROAD IS DECREASED. EMIGRATION OF LATTER GROUP WILL BE GIVEN NEW IMPETUS. THIS LOSS OF TRAINED MANPOWER COULD BE A BRAKE ON ECONOMIC RECOVERY ONCE COPPER PRICES RECOVER. END SUMMARY.

1. DEVALUATION CAME AS NO SURPRISE. SINCE MANY ANTICIPATED THAT GRZ WOULD RESPOND TO RUMORED PRESSURE FROM IMF FOR AROUND 40 PERCENT DEVALUATION, 20 PERCENT CUT CAME ALMOST WITH SENSE OF RELIEF. IN MAKING ANNOUNCEMENT, MINISTER OF FINANCE MWANAKATWE EMPHASIZED DEVALUATION NECESSITATED BY SERIOUS BALANCE OF PAYMENTS SITUATION WHICH NOT EXPECTED TO IMPROVE APPRECIABLY BEFORE 1977 WHEN FOREIGN CREDITS EXPECTED TO EASE PROBLEM AND COPPER PRICES RECOVER. IN ADDITION TO PAYMENTS ARREARAGES ACCUMULATED DURING 1975, PRINCIPALLY FOR IMPORTS, OF APPROXIMATELY \$175 MILLION, MINISTER NOTED THAT ZAMBIA EXPERIENCED ADDITIONALLY \$33 MILLION DEFICIT IN OVERALL BOP ACCOUNT FOR FIRST FIVE MONTHS OF 1976. THIS FOLLOWS BOP DEFICIT IN 1975 OF \$570 MILLION.

2. MAJOR FOREIGN EXCHANGE SAVING WILL FLOW FROM REDUCED FOREIGN EXCHANGE COST OF PAYMENTS FOR INVISIBLES WHICH AMOUNTED TO APPROXIMATELY \$340 MILLION IN 1975, EXCLUSIVE OF FREIGHT AND INSURANCE. SAVINGS ON OUTFLOW OF INVESTMENT INCOME WILL BE ON ORDER OF \$25 MILLION ON ANNUAL BASIS. PRIVATE TRANSFERS, PRIMARILY REMITTANCES OF SALARIES, GRATUITIES AND EMIGRATION ALLOWANCES BY EXPATRIATES WILL BE REDUCED BY AN ESTIMATED \$25 MILLION.
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3. ALTHOUGH GRZ EMPHASIZES BENEFICIAL EFFECT IN ENCOURAGING GREATER USE OF LOCALLY PRODUCED RAW MATERIALS, WE DOUBT THAT GAINS IN SHORT RUN WILL BE SIGNIFICANT. FOR MOST OF ZAMBIA'S INDUSTRIAL PLANT, CHOICE IS TO IMPORT OR DO WITHOUT. SIMILARLY, ZAMBIA'S EXPORT INDUSTRIES ARE UNLIKELY TO FIND THEMSELVES IN MORE COMPETITIVE POSITION SINCE WELL OVER 95 PERCENT OF ZAMBIA'S EXPORTS ARE SOLD AT PRICES DETERMINED

ON COMMODITY MARKETS WHERE VALUE OF KWACHA IS IRRELEVANT. THE FEW ZAMBIAN PRODUCTS WHICH POTENTIALLY MIGHT BENEFIT FROM MORE COMPETITIVE KWACHA RATE PLAY MINISCULE ROLE IN ZAMBIA'S FOREIGN TRADE, AND EVEN THESE PRODUCTS HAVE HIGH IMPORT COMPONENT WHICH WILL FORCE EVENTUAL PRICES INCREASES. MOREOVER, MAJOR IMPEDIMENT TO INCREASED EXPORTS AND/OR IMPORT SUBSTITUTION IS SEVERE IMPORT CUTBACK IN EFFECT SINCE EARLY 1975 WHICH HAS RESULTED IN COMPANIES HAVING TO OPERATE AT UNECONOMIC LEVELS OF PRODUCTION.

4. EFFECT ON PROFITABILITY OF MINING INDUSTRY WILL BE A SHORT TERM BENEFIT OF DEVALUATION. MINING COMPANY OFFICIALS ESTIMATE 70-75 PERCENT OF COPPER PRODUCTION COSTS ARE FOREIGN EXCHANGE RELATED. THUS DEVALUATION WILL REDUCE/TOTAL PRODUCTION COSTS BY PERHAPS 5-10 PERCENT, PRIMARILY IN REDUCED COSTS OF WAGES AND LOCAL INPUTS SUCH AS COAL AND ELECTRICITY. THIS WILL BE ENOUGH TO PLACE THE MINING COMPANIES IN THE BLACK AFTER EXPERIENCING LOSSES APPROACHING \$100 MILLION DURING PAST 12 MONTHS, AND, COUPLED WITH RISE IN PRICE OF COPPER, SHOULD PERMIT THEM TO PROVIDE SOME TAX REVENUE TO THE GRZ.

5. EXPATRIATE AND URBAN ELITE WILL BEAR MAIN BRUNT OF DEVALUATION, BUT PRICE INCREASES WILL AFFECT ALL LEVELS. SINCE VIRTUALLY ALL LOCALLY MANUFACTURED PRODUCTS HAVE A RELATIVELY HIGH IMPORT COMPONENT, PRICE INCREASES WILL BE PERVASIVE AND INEVITABLE ON BOTH IMPORTED AND DOMESTICALLY PRODUCED GOODS. IT IS UNCERTAIN, HOWEVER, HOW LONG GRZ CAN RESIST NEW WAGE DEMANDS. ZAMBIA CONGRESS OF TRADE UNIONS HOLDING EMERGENCY GENERAL COUNCIL MEETING JULY 15 TO DISCUSS EFFECTS ON WORKERS.

6. DEVALUATION IS OF SERIOUS CONCERN TO FOREIGN CONTRACT EMPLOYEES SINCE THEIR REMITTANCES ABROAD WILL BE SHARPLY REDUCED AND THEIR COST OF LIVING IN ZAMBIA INCREASED. THIS WILL LEAD TO THE DEPARTURE OF SOME QUALIFIED PERSONNEL AND WILL REPRESENT

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A CONSTRAINT ON EVENTUAL ECONOMIC RECOVER.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
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Draft Date: 15 JUL 1976
Decaption Date: 01 JAN 1960
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Disposition Approved on Date:
Disposition Authority: ShawDG
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Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
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Document Unique ID: 00
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Enclosure: n/a
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Errors: N/A
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From: LUSAKA
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04 MAY 2006

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